

# AREAS OF RECURRING TAXPAYER NONCOMPLIANCE

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## ■ Returns Processing Center

*Each year the Returns Processing Center of the Indiana Department of Revenue processes well in excess of 5,500,000 tax returns and approximately 3,500,000 payments. It is the Center's goal to process the returns in an efficient manner and to see that payments are deposited and posted in an accurate and timely manner. The Returns Processing Center is an intricate first step in the Department's mission of administering the tax laws in an equitable and courteous manner to promote the highest degree of public trust and voluntary compliance.*

In our efforts to process these returns and payments quickly and efficiently, we have found the following to be areas of recurring taxpayer noncompliance:

### Use of Non-Departmental Payment Coupons

The Department provides preprinted coupon vouchers to taxpayers who are registered with the Department and have a previous history of filing coupons. Relevant tax types include: sales tax, withholding tax, estimated tax for both individuals and corporations, and various other taxes and fees. Each month the Department receives several thousand payments without coupons, maybe with handwritten information on pieces of paper, coupons from prior filing periods that have been changed to fit the periods for which the taxpayers are trying to file, or just payments with no explanation.

### Failure to Complete All the Required Lines/Information

The Department receives numerous returns that are not completed by the taxpayer, which delays their processing and necessitates Department personnel's having to complete the form based on the information provided, contacting the taxpayer, or returning the form to the taxpayer for additional information. These problems slow down the Department's ability to process returns quickly and efficiently.

### Filing the Wrong Return

The Department receives numerous returns each year

which are on the correct forms but not for the current year, or may be for the correct year but are on the wrong forms. An example would be taxpayers' submitting IT-40EZ forms when they do not qualify for that form because of the type of income or deductions they may have. In these cases, Department employees must determine the correct form to be used and either attempt to transfer the information to the correct form, or return the form submitted along with a copy of the correct form to the taxpayer for resubmitting.

### Failure to Attach W-2 Forms

The Department receives a vast number of Individual Income Tax returns without W-2 forms to verify the withholding taxes taken as credits on the returns. Failure to submit W-2 forms causes the returns to be rejected and returned to taxpayers with requests for correct documentation.

### Failure to Attach W-2 Forms with the WH-3

The WH-3 is a reconciliation of the W-2 forms; and, both the WH-3 and all W-2 forms must be submitted together annually. The Department often receives WH-3 forms without W-2 forms attached. It also often finds cases of taxpayers changing business names during the year but continuing to file their taxes under their previous Identification Number, and then using the incorrect forms at the end of the year to submit their withholding information for the year.

### Failure to Attach the Necessary Schedules

The Department finds that often taxpayers take credits on their tax returns, but fail to include documentation or necessary schedules to substantiate the deduction or credits being taken (e.g. College Credit, Form CC 40).

### Failure to Comply with Enterprise Zone Deduction

If taxpayers live in an Enterprise Zone and work for a qualified employer in that zone, they may be qualified to take this deduction. The deduction is one-half (1/2) of the earned income shown on form IT-40QEC, or \$7,500, whichever is less. Often the deduction is calculated incorrectly, or Form IT-40QEC, which should

be provided and completed by the employer, is not attached to the taxpayers' Form IT-40.

### Taxpayer Filing Wrong Form

Taxpayers who are residents from Reciprocal States often file on Indiana Form IT-40 and take a deduction of the other state's income, rather than filing the appropriate Indiana Form IT-40RNR (Reciprocal Nonresident).

### Penalty for Underpayment of Estimated Tax

Taxpayers often owe penalties for underpayment of estimated taxes if they didn't have taxes withheld from their income and/or didn't pay sufficient estimated taxes throughout the year. Generally speaking, if a taxpayer owes \$400.00 or more in state and county taxes for the year that are not covered by withholding taxes, the taxpayer needs to begin making estimated tax payments.

### Failure to Calculate County Tax

Often taxpayers fail to compute their county taxes. If, on January 1, 1998, taxpayers lived and/or worked in an Indiana county that has a tax, they must figure their county tax. Failure to calculate county tax due may delay processing of their returns.

## ■ Compliance Division

***The Indiana Department of Revenue's Compliance Division researches, develops, tests and implements various projects to identify non-filing, non-complying taxpayers in the areas of individual, corporate, sales/use, and withholding taxes. Outreach through educational seminars and programs is conducted in an effort to promote "voluntary" compliance by Indiana taxpayers.***

### AERONAUTICS SECTION

The Aeronautics Section mailed 4,522 aircraft registration renewals for the calendar year 1998. As of December 31, 1998, 180 aircraft were delinquent. This translates to a 96% compliance rate. The following amounts were collected and processed by the Aeronautics Section for the Fiscal Year 1998 – 1999:

Aircraft Sales/Use Tax	\$1,487,006.00
Aircraft Excise Tax	\$ 408,924.00
Registration Fees	\$ 49,070.00
<b>Total</b>	<b>\$1,945,000.00</b>

According to Indiana Code (6-6-6.5), airport owners who fail to report to the Department all aircraft based at their facility are subject to a late penalty of \$10.00 per day. Penalties totaling \$2,120 were collected from delinquent airports in FY99. These reports are used to verify that all aircraft owners based in Indiana are in compliance with Indiana registration laws.

Indiana Code was changed, effective January 1, 1999, to limit the amount of time an aircraft dealer is allowed to hold aircraft as tax-exempt inventory "for resale" to eighteen (18) months from the purchase date. Aircraft dealers holding aircraft longer than eighteen (18) months will be subject to all applicable taxes of an aircraft owner.

### BANKRUPTCY/RESPONSIBLE OFFICER SECTION

The Bankruptcy Section receives notification from federal district courts of bankruptcies related to the State of Indiana. The State file proofs of claims with the courts of any outstanding Indiana tax liabilities. During the Fiscal Year 1999, this Section filed 1,790 claims with the U.S. Bankruptcy Courts, totaling \$15,273,819.00 in unpaid tax delinquencies and projected tax liabilities for non-filed returns.

Trust fund taxes are comprised predominantly of sales and withholding taxes. Individuals who are employees or officers of corporations and who have a duty to remit trust taxes to the Department of Revenue are personally liable for the payment of these taxes. During the Fiscal Year 1999, responsible officers were assessed \$3,649,112.00 in delinquent trust taxes.

### CHARITY GAMING/NOT-FOR-PROFIT SECTION

This Section is responsible for determining organizations' not-for-profit status and for licensing qualified not-for-profit organizations for bingo, festivals, raffles, door prizes, and charity game nights. The licensing of manufacturers and distributors to sell tip boards, punch boards, and pull tabs is performed in this Section.

A total of \$4,170,334.00 in fees was collected from the following licenses issued:

<u>Type of License</u>	<u>Number of Licenses Issued</u>
Annual Bingo	1,032
Charity Game Night	282
Door Prize	8
Festival	303
Raffle	517
Special Bingo	137
<b>Total Licenses Issued</b>	<b>2,279</b>

Gaming License Fees	\$ 4,015,334.00
Manufacturers License	\$ 33,000.00
Distributors License	\$ 122,000.00
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Total License Fees	\$ 4,170,334.00

## **CORPORATE INCOME TAX SECTION**

This Section handles a variety of tax issues as they relate to corporations, partnerships, financial institutions, and governmental entities. It provides assistance to taxpayers with telephone and/or written inquiries related to gross, adjusted gross, and supplemental net income taxes, as well as forms, schedules, deductions, credits and liabilities.

### **Corporation/Partnership Agreed**

Agreed federal audit reports are provided to the Department by the Internal Revenue Service. If taxpayers have not filed amended returns with the Department to report the federal audit changes, assessments are created. For Fiscal Year 1999, this project generated total tax liabilities of \$1,651,186.00.

### **Voluntary Compliance Agreements**

Voluntary compliance agreements occur when a taxpayer initiates contact with the Department to become compliant with Indiana filing requirements. This program resulted in collections of \$797,116.00 during FY99.

### **Penalty for Underpayment of Estimated Tax/ Late Payment Penalty**

This project involves reviewing tax returns filed by taxpayers who either did not make any quarterly estimated income tax payments or omitted one or more quarterly payments during the tax year.

## **INDIVIDUAL/WITHHOLDING TAX SECTION**

The Individual Income Tax Section's mission is to identify and pursue non-filers, as well as to verify the accuracy of filed returns. These functions are performed by utilizing information from the Internal Revenue Service, various Indiana state agencies, other state taxing agencies, and anonymous informants. Our standard compliance projects and findings for Fiscal Year 1999 are as follows:

## **Federal Audits**

The Internal Revenue Service provides agreed federal tax audit reports to the Department. If taxpayers do not amend their Indiana individual income tax return to report the Indiana adjustments resulting from the federal modifications detailed in the audit findings, a tax assessment is generated. This project resulted in 2,272 taxpayers being assessed a total of \$2,261,925.00.

## **CP2000 Unreported Income**

The Department receives data from the Internal Revenue Service regarding taxpayers who failed to report all taxable income. This could be income derived from wages, interest, dividends, or non-employee compensation. These types of income are reported on W-2's or Form 1099 information returns. An assessment is generated if the income was not reported on the original return, or an amended return. The project resulted in 3,017 taxpayer assessments totaling \$543,175.00.

## **Withholding Discrepancies**

A comparison is made between taxpayers' annual WH-3 Forms with the state and county withholding payments (from Form WH-1) made during the year. If underpayments exist, taxpayers are assessed the differences. The project resulted in 1,466 taxpayers being assessed \$2,956,829.00.

## **Individual Desk Audits**

Individual Desk Audits resulted in 75 assessments totalling \$63,291.00. These audits were conducted from submissions within the Department, as well as from anonymous sources.

## **STRATEGIC COMPLIANCE SECTION**

The Strategic Section of the Compliance Division researches, develops, and implements projects designed to increase taxpayer education and voluntary compliance. This staff also assists other areas, eliminating processing backlogs by completing various types of correspondence, examining tax returns for accuracy, and researching returned mail for the most current addresses available.

## **Corporate/Individual Use Tax**

This section continues to focus on informing professional and service-oriented businesses, as well as individual taxpayers, that they may have a use tax liability. The educational effort was successful and generated collections of \$187,876.00.

Approximately \$220,000.00 was collected from a variety of sources. Assessments were generated from information received from the Bureau of Motor Vehicles and from other states. Payments were received from out-of-state companies who either owed Indiana use tax or had collected Indiana sales tax from an Indiana customer.

## **Account Examination**

Taxpayer accounts (income, sales, withholding, food and beverage, county innkeepers, etc.) are researched to determine delinquent tax. This research produced \$179,392.00.

## **Withholding**

Through the Federal/State Exchange Agreement, the Internal Revenue Service provides the Indiana Department of Revenue with information on employers who have filed paper W-2 returns with the IRS and have a link with Indiana. This resulted in assessments totaling \$591,355.00 in FY99.

This Section also reviews information on potential non-filers for individual income tax, sales tax, withholding tax, and corporate income tax. Miscellaneous projects from various sources collected an additional \$4,385,013.00.

## **UTILITY/REFUND SECTION**

This section reviewed and processed 7,204 Applications for Utility Sales Tax Exemption (Form ST-200) and 2,912 claims for refund of sales tax, totaling \$14,395,910.00. Refunds claimed were reduced by \$4,601,120.00 as a result of taxpayer failure to meet exemption requirements, taxpayer failure to sufficiently document claims, and the expiration of the Statute of Limitations.

## **Voluntary Compliance**

Compliance agreements occur when taxpayers initiate contact with the Department about their delinquent tax status. The taxpayers may either be unaware of State filing requirements or, for some other reason, have not filed tax returns. Collections from this project totaled \$868,375.00 for FY99.